

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF BENNY JONES WATER	)	
SUPPLY CO., INC. FOR A RATE ADJUSTMENT	)	CASE NO.
PURSUANT TO THE ALTERNATIVE RATE	)	92-339
FILING PROCEDURE FOR SMALL UTILITIES	)	

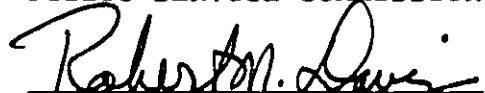
O R D E R

On August 17, 1992, Benny Jones Water Supply Co., Inc. ("Benny Jones") filed its application for Commission approval to increase its water rates. Commission Staff, having performed a limited financial review of Benny Jones' operations, has prepared the attached Staff Report containing Staff's findings and recommendations regarding the proposed rates. All parties should review the report carefully and provide any written comments or requests for a hearing or informal conference no later than 15 days from the date of this Order.

IT IS THEREFORE ORDERED that all parties shall have 15 days from the date of this Order to provide written comments regarding the attached Staff Report or requests for a hearing or informal conference. If no request for a hearing or informal conference is received, then this case will be submitted to the Commission for a decision.

Done at Frankfort, Kentucky, this 20th day of November, 1992.

PUBLIC SERVICE COMMISSION

  
For the Commission

ATTEST:

  
Executive Director

COMMONWEALTH OF KENTUCKY  
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THE APPLICATION OF BENNY JONES	)	
WATER SUPPLY CO., INC. FOR A	)	
RATE ADJUSTMENT PURSUANT TO THE	)	CASE NO. 92-339
ALTERNATIVE RATE FILING PROCEDURE	)	
FOR SMALL UTILITIES	)	

STAFF REPORT

Prepared By: Mark C. Frost  
Public Utility Financial  
Analyst, Chief  
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Public Utility Rate Analyst, Sr.  
Communications, Water  
and Sewer Rate Design Branch  
Research Division

STAFF REPORT

ON

BENNY JONES WATER SUPPLY CO., INC.

CASE NO. 92-339

A. Preface

On August 17, 1992, Benny Jones Water Supply Co., Inc. ("Benny Jones") filed its application seeking approval to increase its rates pursuant to the Alternative Rate Filing Procedure for Small Utilities ("ARF"). Benny Jones proposed rates which would produce an increase in its annual revenues of \$4,020, an increase of 71.8 percent over test-period normalized revenues from rates of \$5,600.

In order to evaluate the requested increase, the Commission Staff ("Staff") chose to perform a limited financial review of Benny Jones' operations for the test-period, the calendar year ending December 31, 1991. Since Benny Jones requested and received Staff assistance in filing its ARF application, the field review was performed prior to the filing of the application.

Benny Jones provided Staff with its general ledger, canceled checks, and invoices. Using this information, Mark C. Frost of the Commission's Division of Rates and Tariffs performed the limited review at the Commission's offices in Frankfort, Kentucky. George Stienmetz of the Commission's Division of Research prepared the billing analysis during this same month.

Mr. Frost is responsible for the preparation of this Staff Report except for Section B, Operating Revenues; Section D, Rate Design; Section E, Non-Recurring Charges; and Appendix A, which were prepared by Mr. Steinmetz. Based on the findings contained in

this report, Staff recommends that Benny Jones be allowed to increase its annual revenues from water sales by \$3,279.

### Scope

The scope of the review was limited to obtaining information as to whether the test-period operating revenues and expenses were representative of normal operations. Insignificant or immaterial discrepancies were not pursued and are not addressed herein.

### B. Analysis of Operating Revenues and Expenses

#### Operating Revenues

In Exhibit 1 of the application, Benny Jones reported operating revenues from unmetered water sales during the test year in the amount of \$3,288. The existing rates should produce normalized revenues from unmetered water sales of \$5,600.<sup>1</sup>

#### Operating Expenses

Benny Jones reported actual and pro forma operating expenses of \$3,926 and \$7,847, respectively. The following are Staff's recommended adjustments to Benny Jones' actual test-period operations:

Owner/Manager Fee: Benny Jones did not incur an owner/manager fee during the test-period, however it did propose to include an

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<sup>1</sup> Test Year Customers:  
19 permanent homes + 21 mobile homes = 40 Individuals

Present Annual Rate	\$ 125
Times: Individuals	x 40
Subtotal	\$ 5,000
Plus: Marina Annual Rate	+ 600
Adjusted Revenue	<u>\$ 5,600</u>

owner/manager fee of \$2,400 in pro forma operations. Benny Jones' request is based on the Commission's past practice of allowing owner/manager fees of \$2,400 for utilities of similar size.

Staff is of the opinion that Benny Jones is entitled to an owner/manager fee and based on the Commission's past practice, the proposed level of \$2,400 is reasonable. Accordingly, operating expenses have been increased by \$2,400.

Testing: Benny Jones proposed a pro forma level of testing expense of \$240, an increase of \$47 above its test-period level. Benny Jones pays a testing fee of \$20 per month or \$240 annually, which is the basis for this adjustment.

Since an adjustment based on the current testing fee meets the rate-making criteria of known and measurable, Staff recommends that Benny Jones' adjustment be accepted. Accordingly, testing expense has been increased by \$47.

Postage: Benny Jones proposed a pro forma level of postage expense of \$81, an increase of \$10 above its test-period level. Benny Jones' adjustment is based on including the cost of mailing items to the Commission that were mistakenly excluded from its test-period operations.

Upon review of the canceled checks and invoices, Staff determined test-period postage expense was understated by \$10 and therefore, postage expense has been increased by that amount.

Telephone: Benny Jones proposed a pro forma level of telephone expense of \$8, a decrease of \$15 from its test-period level.

Benny Jones' office is maintained in Dayton, Ohio for the benefit of Sharon Roe, Benny Jones' manager and daughter of the owner. The decision to locate Benny Jones' office in Dayton, Ohio was a management decision that benefits Benny Jones and not its rate-payers. Therefore, the ratepayers should not bear the cost that resulted from management's decision, which is the basis for Benny Jones' adjustment.

Staff is in agreement with Benny Jones that the rate-payers should not bear this cost and therefore, recommends that test-period expenses be reduced by \$15.

Legal: Benny Jones incurred legal fees of \$661 in the test-period which represented its cost to incorporate. Benny Jones proposed to remove its legal fees from test-period operations and amortize them over a 20 year period, the estimated life of its treatment plant. This resulted in a net reduction to test-period operations of \$628.<sup>2</sup>

Staff is of the opinion that Benny Jones' proposed treatment of legal fees is correct and that the proposed amortization period is reasonable. Accordingly, legal fees of \$661 have been

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<sup>2</sup>

Legal Fees	\$ 661
Amortization    \$ 661 ÷ 20-Years =	- 33
Net Test-Period Operation Reduction	<u>\$ 628</u>

eliminated from and amortization expense of \$33 has been included in test-period operations.

Complaint/Initial Rates Case: Benny Jones attended the hearing in Case No. 90-312<sup>3</sup> that was held at the Commission's offices in Frankfort, Kentucky at a cost of \$71, which is included in Benny Jones' test-period operations. This adjustment reflects the elimination of the \$71 from test-period operations and the amortization of this amount over a 3 year period. This would result in a net reduction to test-period operations of \$47.<sup>4</sup>

The Commission's past practice has been to amortize the cost of nonrecurring cases (i.e., administrative and rate) over a 3 year period. Based on this past practice, Staff recommends that Benny Jones' adjustment be accepted. Therefore, test-period operations has been reduced by \$71 and amortization expense increased by \$24.

Mileage: Benny Jones proposed to eliminate its test-period transportation expense of \$526. This expense represented the mileage reimbursement paid to Ms. Roe. As with telephone expense, the mileage reimbursement represents a cost that resulted from a management decision to locate Benny Jones' office in Dayton, Ohio. This expense should not be borne by the ratepayers and therefore,

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<sup>3</sup> Case No. 90-312, Robert C. Jones, Complainant Vs. Benny Jones Water Supply, Defendant, Order entered June 17, 1991.

<sup>4</sup>

Cost of Last Case	\$ 71
Amortization \$71 ÷ 3-Years =	- 24
Net Effect to Test-Period Operations	<u>\$ 47</u>

Benny Jones proposed to eliminate this expense from its test-period operations.

Staff is in agreement that this cost should not be borne by the ratepayers and therefore, test-period expenses have been reduced by \$526.

Volatile Synthetic Organic Chemical Testing: Benny Jones proposed a pro forma level of Volatile Synthetic Organic Chemical ("VOCs") testing expense of \$900. In 1992 the Natural Resources and Environmental Protection Cabinet ("Natural Resources") ordered Benny Jones to perform a year of quarterly VOCs testing that is to be repeated every 3 years. Benny Jones' adjustment reflects amortizing the annual VOCs testing cost of \$2,700 over a 3-year period.

Benny Jones performed its VOCs testing to comply with a Natural Resources requirement. An adjustment to reflect Benny Jones' cost to comply with a Natural Resources requirement would meet the rate-making criteria of known and measurable. However, Fouser Environmental Service's ("Fouser") invoice of May 17, 1992, showed that its VOCs testing fee is \$225 per quarter or \$900 annually, which would result in an amortization expense of \$300<sup>5</sup> and not \$900 as Benny Jones proposed.

Upon review of the Natural Resources letter and the Fouser invoice, Staff is of the opinion that the annual VOCs testing cost of \$900 is reasonable and the proposed 3-year amortization period

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<sup>5</sup>  $\$900 \div 3 \text{ Years} = \$300.$



is appropriate. Accordingly, amortization expense has been increased by \$300.

Depreciation: In 1992, Natural Resources fined Benny Jones for non-compliance with its operating guidelines and required Benny Jones to upgrade/expand the treatment facility. To cooperate with Natural Resources, Benny Jones installed a new filtration system and a sump pump, and repaired a pump.

Benny Jones proposed to depreciate the cost to install its filtration system of \$7,842 over a 5-year period, and to depreciate its pump installation of \$561 and pump repair of \$284 over 3-years. This results in a pro forma depreciation expense of \$1,850,<sup>6</sup> an increase of \$1,780 above Benny Jones' reported depreciation expense.

Staff reviewed the Natural Resources letter of September 27, 1992, and determined that Benny Jones was required to construct its plant improvements. As with VOCs testing, the cost Benny Jones incurred to comply with a Natural Resources' guideline is known and measurable.

Staff has reviewed Benny Jones' adjustment and is of the opinion that both the cost of the improvements and proposed depreciation lives are reasonable. Therefore, depreciation expense has been increased by \$1,780.

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<sup>6</sup>

Filtration System	\$ 7,842 + 5-Years	= \$ 1,568
Pump Installation	\$ 561 + 3-Years	= 187
Pump Repair	\$ 284 + 3-Years	= + 95
Pro Forma Depreciation Expense		<u>\$ 1,850</u>

### Operations Summary

Based on the recommendations of Staff contained in this report, Benny Jones' operating statement would appear as set forth in Appendix B to this report.

### C. Revenue Requirements Determination

The approach frequently used by this Commission to determine revenue requirements for small, privately-owned utilities is the operating ratio. This approach is used primarily when there is no basis for rate-of-return determination or the cost of the utility has fully or largely been recovered through the receipt of contributions. Staff recommends the use of this approach in determining Benny Jones' revenue requirement.

Staff's adjusted operations provide Benny Jones with an operating ratio of 129.41 percent.<sup>7</sup> Combined with Benny Jones' requested increase of \$4,020 the result is an operating ratio of 75.33 percent.<sup>8</sup>

Benny Jones has requested an operating ratio of 88 percent. Staff is of the opinion that this would allow Benny Jones' sufficient revenues to cover its operating expenses, and to provide for reasonable equity growth. An operating ratio of 88 percent and an allowance for the appropriate state and federal income taxes

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<sup>7</sup>  $\$7,247 \div \$5,600 = 129.41\%$ .

<sup>8</sup>  $\$7,247 \div (\$5,600 + \$4,020) = 75.33\%$ .

results in a revenue requirement of \$8,879.<sup>9</sup> Therefore, Staff recommends that Benny Jones be allowed to increase its annual operating revenues by \$3,279.<sup>10</sup>

D. Rate Design

Benny Jones filed as part of the application a schedule of its existing and proposed rates. Benny Jones did not propose a change in its present rate design. Benny Jones did propose across the board increases to all categories of customers of 72 percent.

Cost allocation and rate design are related processes. The purpose of analyzing costs is to provide a basis for setting rates. Most of the increased costs in this case result from depreciation of plant and compensating management for running the system, therefore any increase granted in this case has been passed on at an equal percentage to all categories of customers using the existing rate schedule. The rates in Appendix A will produce the revenue required.

<sup>9</sup>	Adjusted Operating Expenses	\$	7,247
	Requested Operating Ratio	+	88%
	Subtotal	\$	8,235
	Less: Adjusted Operating Exp.	-	7,247
	Required Margin After Income Tax	\$	988
	Times: Gross-Up Factor	x	1.651391297
	Required Margin Before Income Tax	\$	1,632
	Add: Adjusted Operating Exp.	+	7,247
	Required Operating Revenue	\$	<u>8,879</u>
<sup>10</sup>	Required Operating Revenue	\$	8,879
	Less: Normalized Operating Rev.	-	5,600
	Required Revenue Increase	\$	<u>3,279</u>

Addressing the lack of meters in Benny Jones, pursuant to 807 KAR 5:006 Section 10(3), Benny Jones needs to be able to monitor its customers' usage at least annually. Staff recommends that meters be installed so all customers' usage can be monitored to promote conservation and forestall the need for further plant construction.

E. Non-Recurring Charges

Benny Jones filed cost justification relating to various non-recurring charges. Benny Jones requested a 10 percent late payment, a \$20 reconnect fee after disconnection due to nonpayment, a \$20 disconnection fee resulting from a leak on the customer's portion of the line, and a returned check charge of \$20.

Staff agrees that the cost justification provided by Benny Jones for the non-recurring charges is adequate and therefore recommends that these proposed charges be approved.

F. Signatures

Mark C. Frost  
Prepared By: Mark C. Frost  
Public Utility Financial  
Analyst, Chief  
Water and Sewer Revenue  
Requirements Branch  
Rates and Tariffs Division

George R. Steinmetz  
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Public Utility Rate  
Analyst, Sr.  
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and Sewer Rate Design Branch  
Research Division

**APPENDIX A**  
**TO STAFF REPORT CASE NO. 92-339**

The Staff recommends the following rate be prescribed for customers of Benny Jones Water Supply Company.

Individual (Annual)	\$ 198.20
Marina (Annual)	\$ 951.00

APPENDIX B  
TO STAFF REPORT CASE NO. 92-339

	Actual Test-Period Operations -----	Pro Forma Adjustments -----	Adjusted Operations -----
Operating Revenue:			
Unmetered Water Sales	\$ 3,288	\$ 2,312	\$ 5,600
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Operating Expenses:			
Owner/Management Fee	0	2,400	2,400
Electric Expense	822	0	822
Testing Expense	193	47	240
Chemicals - Bleach	220	0	220
Testing Supplies	156	0	156
Sand - Filtration System	132	0	132
Postage Expense	71	10	81
Contract Labor	395	0	395
Office Supplies	20	0	20
Telephone Calls	23	(15)	8
Legal Services	661	(661)	0
Copies	26	0	26
Miscellaneous Expense	249	0	249
Trip to Frankfort	71	(71)	0
Milage	526	(526)	0
Licenses & Taxes	282	0	282
Bank Charges - Checks	9	0	9
Depreciation Expense	70	1,780	1,850
Amortization Expense	0	357	357
Income Taxes	0	0	0
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Total Operating Expenses	\$ 3,926	\$ 3,321	\$ 7,247
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Net Income/(Loss)	\$ (638)	\$ (1,009)	\$ (1,647)
	=====	=====	=====